APPLE INC
Form 10-Q
April 28, 2015
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 28, 2015

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ______ to ______.

Commission File Number: **001-36743**

Apple Inc.

(Exact name of Registrant as specified in its charter)

California	**94-2404110**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1 Infinite Loop	
Cupertino, California	**95014**
(Address of principal executive offices)	(Zip Code)

(408) 996-1010

(Registrant s telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files).

Yes x No ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

5,761,030,000 shares of common stock, par value $0.00001 per share, issued and outstanding as of April 10, 2015

Table of Contents

Apple Inc.

Form 10-Q

For the Fiscal Quarter Ended March 28, 2015

TABLE OF CONTENTS

Table of Contents

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(In millions, except number of shares which are reflected in thousands and per share amounts)

	Three Months Ended		Six Months Ended	
	March 28, 2015	March 29, 2014	March 28, 2015	March 29, 2014
Net sales	$ 58,010	$ 45,646	$ 132,609	$ 103,240
Cost of sales	34,354	27,699	79,212	63,447
Gross margin	23,656	17,947	53,397	39,793
Operating expenses:				
Research and development	1,918	1,422	3,813	2,752
Selling, general and administrative	3,460	2,932	7,060	5,985
Total operating expenses	5,378	4,354	10,873	8,737
Operating income	18,278	13,593	42,524	31,056
Other income/(expense), net	286	225	456	471
Income before provision for income taxes	18,564	13,818	42,980	31,527
Provision for income taxes	4,995	3,595	11,387	8,232
Net income	$ 13,569	$ 10,223	$ 31,593	$ 23,295
Earnings per share:				
Basic	$ 2.34	$ 1.67	$ 5.43	$ 3.76
Diluted	$ 2.33	$ 1.66	$ 5.39	$ 3.74
Shares used in computing earnings per share:				
Basic	5,793,799	6,123,302	5,818,441	6,197,903
Diluted	5,834,858	6,156,699	5,858,330	6,233,430

Cash dividends declared per share	$ 0.47	$ 0.44	$ 0.94	$ 0.88

See accompanying Notes to Condensed Consolidated Financial Statements.

3

Table of Contents

Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(In millions)

	Three Months Ended		Six Months Ended	
	March 28, 2015	**March 29, 2014**	**March 28, 2015**	**March 29, 2014**
Net income	$ 13,569	$ 10,223	$ 31,593	$ 23,295
Other comprehensive income:				
Change in foreign currency translation, net of tax	(180)	(19)	(246)	(86)
Change in unrealized gains/losses on derivative instruments:				
Change in fair value of derivatives, net of tax	1,037	(109)	3,019	104
Adjustment for net (gains)/losses realized and included in net income, net of tax	(739)	(13)	(1,304)	59
Total change in unrealized gains/losses on derivative instruments, net of tax	298	(122)	1,715	163
Change in unrealized gains/losses on marketable securities:				
Change in fair value of marketable securities, net of tax	593	235	137	193
Adjustment for net (gains)/losses realized and included in net income, net of tax	36	(39)	22	(50)
Total change in unrealized gains/losses on marketable securities, net of tax	629	196	159	143
Total other comprehensive income	747	55	1,628	220
Total comprehensive income	$ 14,316	$ 10,278	$ 33,221	$ 23,515

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

Apple Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

(In millions, except number of shares which are reflected in thousands and par value)

	March 28, 2015	September 27, 2014
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 14,489	$ 13,844
Short-term marketable securities	18,607	11,233
Accounts receivable, less allowances of $83 and $86, respectively	10,905	17,460
Inventories	2,396	2,111
Deferred tax assets	5,141	4,318
Vendor non-trade receivables	7,259	9,759
Other current assets	9,094	9,806
Total current assets	67,891	68,531
Long-term marketable securities	160,443	130,162
Property, plant and equipment, net	20,151	20,624
Goodwill	4,711	4,616
Acquired intangible assets, net	4,061	4,142
Other assets	3,937	3,764
Total assets	$ 261,194	$ 231,839
LIABILITIES AND SHAREHOLDERS EQUITY:		
Current liabilities:		
Accounts payable	$ 23,159	$ 30,196
Accrued expenses	22,827	18,453
Deferred revenue	8,944	8,491
Commercial paper	3,799	6,308
Total current liabilities	58,729	63,448
Deferred revenue non-current	3,571	3,031
Long-term debt	40,072	28,987
Other non-current liabilities	29,816	24,826
Total liabilities	132,188	120,292

Commitments and contingencies				
Shareholders equity:				
Common stock and additional paid-in capital, $0.00001 par value: 12,600,000 shares authorized; 5,762,278 and 5,866,161 shares issued and outstanding, respectively		25,376		23,313
Retained earnings		100,920		87,152
Accumulated other comprehensive income		2,710		1,082
Total shareholders equity		129,006		111,547
Total liabilities and shareholders equity	$	261,194	$	231,839

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(In millions)

	Six Months Ended	
	March 28, 2015	**March 29, 2014**
Cash and cash equivalents, beginning of the period	$ 13,844	$ 14,259
Operating activities:		
Net income	31,593	23,295
Adjustments to reconcile net income to cash generated by operating activities:		
Depreciation and amortization	5,054	4,031
Share-based compensation expense	1,815	1,377
Deferred income tax expense	1,879	2,059
Changes in operating assets and liabilities:		
Accounts receivable, net	6,555	3,401
Inventories	(285)	(65)
Vendor non-trade receivables	2,500	1,419
Other current and non-current assets	2,448	14
Accounts payable	(5,428)	(2,375)
Deferred revenue	993	1,414
Other current and non-current liabilities	5,679	1,638
Cash generated by operating activities	52,803	36,208
Investing activities:		
Purchases of marketable securities	(92,523)	(90,360)
Proceeds from maturities of marketable securities	5,871	10,869
Proceeds from sales of marketable securities	48,924	80,241
Payments made in connection with business acquisitions, net	(115)	(559)
Payments for acquisition of property, plant and equipment	(5,586)	(3,367)
Payments for acquisition of intangible assets	(155)	(163)
Other	88	(23)
Cash used in investing activities	(43,496)	(3,362)
Financing activities:		
Proceeds from issuance of common stock	309	341
Excess tax benefits from equity awards	357	363
Taxes paid related to net share settlement of equity awards	(608)	(430)

Dividends and dividend equivalents paid		(5,544)		(5,430)
Repurchase of common stock		(12,000)		(23,000)
Proceeds from issuance of long-term debt, net		11,332		0
Repayments of commercial paper, net		(2,508)		0
Cash used in financing activities		(8,662)		(28,156)
Increase in cash and cash equivalents		645		4,690
Cash and cash equivalents, end of the period	$	14,489	$	18,949
Supplemental cash flow disclosure:				
Cash paid for income taxes, net	$	7,058	$	5,369
Cash paid for interest	$	220	$	161

See accompanying Notes to Condensed Consolidated Financial Statements.

Apple Inc.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 Summary of Significant Accounting Policies

Apple Inc. and its wholly-owned subsidiaries (collectively Apple or the Company) designs, manufactures and markets mobile communication and media devices, personal computers and portable digital music players, and sells a variety of related software, services, accessories, networking solutions and third-party digital content and applications. The Company sells its products worldwide through its retail stores, online stores and direct sales force, as well as through third-party cellular network carriers, wholesalers, retailers and value-added resellers. In addition, the Company sells a variety of third-party iPhone, iPad, Mac and iPod compatible products, including application software, and various accessories through its online and retail stores. The Company sells to consumers, small and mid-sized businesses and education, enterprise and government customers.

Basis of Presentation and Preparation

The accompanying condensed consolidated financial statements include the accounts of the Company. Intercompany accounts and transactions have been eliminated. The preparation of these condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in these condensed consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates.

These condensed consolidated financial statements and accompanying notes should be read in conjunction with the Company s annual consolidated financial statements and the notes thereto for the fiscal year ended September 27, 2014, included in its Annual Report on Form 10-K as updated by the Company s Current Report on Form 8-K dated January 28, 2015 (hereinafter, the 2014 Form 10-K). The Company s fiscal year is the 52 or 53-week period that ends on the last Saturday of September. An additional week is included in the first fiscal quarter approximately every six years to realign fiscal quarters with calendar quarters. The Company s fiscal years 2015 and 2014 each include 52 weeks. Unless otherwise stated, references to particular years, quarters or months refer to the Company s fiscal years ended in September and the associated quarters or months of those fiscal years.

Earnings Per Share

Basic earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during the period increased to include the number of additional shares of common stock that would have been outstanding if the potentially dilutive securities had been issued. Potentially dilutive securities include outstanding stock options, shares to be purchased under the Company s employee stock purchase plan, unvested restricted stock and unvested restricted stock units (RSUs). The dilutive effect of potentially dilutive securities is reflected in diluted earnings per share by application of the treasury stock method. Under the treasury stock method, an increase in the fair market value of the Company s common stock can result in a greater dilutive effect from potentially dilutive securities.

The following table shows the computation of basic and diluted earnings per share for the three- and six-month periods ended March 28, 2015 and March 29, 2014 (net income in millions and shares in thousands):

	Three Months Ended		Six Months Ended	
	March 28, 2015	**March 29, 2014**	**March 28, 2015**	**March 29, 2014**
Numerator:				
Net income	$ 13,569	$ 10,223	$ 31,593	$ 23,295
Denominator:				
Weighted-average shares outstanding	5,793,799	6,123,302	5,818,441	6,197,903
Effect of dilutive securities	41,059	33,397	39,889	35,527
Weighted-average diluted shares	5,834,858	6,156,699	5,858,330	6,233,430
Basic earnings per share	$ 2.34	$ 1.67	$ 5.43	$ 3.76
Diluted earnings per share	$ 2.33	$ 1.66	$ 5.39	$ 3.74

Potentially dilutive securities, whose effect would have been antidilutive, were not significant for the three- and six-month periods ended March 28, 2015 and the three- and six-month periods ended March 29, 2014. The Company excluded these securities from the computation of diluted earnings per share.

Table of Contents

Note 2 Financial Instruments

Cash, Cash Equivalents and Marketable Securities

The following tables show the Company s cash and available-for-sale securities adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category recorded as cash and cash equivalents or short- or long-term marketable securities as of March 28, 2015 and September 27, 2014 (in millions):

	March 28, 2015						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-Term Marketable Securities	Lon Mar Sec
	$ 9,879	$ 0	$ 0	$ 9,879	$ 9,879	$ 0	$
:							
rket funds	1,457	0	0	1,457	1,457	0	
nds	2,384	0	(126)	2,258	0	2,258	
	3,841	0	(126)	3,715	1,457	2,258	
:							
ury securities	42,854	145	(12)	42,987	0	1,791	
cy securities	6,901	11	(2)	6,910	585	1,056	
government securities	7,114	86	(80)	7,120	41	271	
s of deposit and time deposits	3,473	0	0	3,473	1,163	1,252	
al paper	2,956	0	0	2,956	1,364	1,592	
securities	100,658	427	(370)	100,715	0	10,325	
securities	942	5	(1)	946	0	24	
and asset-backed securities	14,782	75	(19)	14,838	0	38	
	179,680	749	(484)	179,945	3,153	16,349	
	$ 193,400	$ 749	$ (610)	$ 193,539	$ 14,489	$ 18,607	$

	September 27, 2014						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-Term Marketable Securities	Lon Mar Sec
	$ 10,232	$ 0	$ 0	$ 10,232	$ 10,232	$ 0	$
:							

rket funds	1,546	0	0	1,546	1,546	0	
nds	2,531	1	(132)	2,400	0	2,400	
	4,077	1	(132)	3,946	1,546	2,400	
:							
ury securities	23,140	15	(9)	23,146	12	607	
y securities	7,373	3	(11)	7,365	652	157	
government securities	6,925	69	(69)	6,925	0	204	
s of deposit and time deposits	3,832	0	0	3,832	1,230	1,233	
al paper	475	0	0	475	166	309	
securities	85,431	296	(241)	85,486	6	6,298	
securities	940	8	0	948	0	0	
and asset-backed securities	12,907	26	(49)	12,884	0	25	
	141,023	417	(379)	141,061	2,066	8,833	
	$ 155,332	$ 418	$ (511)	$ 155,239	$ 13,844	$ 11,233	$

(1) The fair value of Level 1 securities is estimated based on quoted prices in active markets for identical assets or liabilities.

(2) The fair value of Level 2 securities is estimated based on observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Table of Contents

The Company may sell certain of its marketable securities prior to their stated maturities for strategic reasons including, but not limited to, anticipation of credit deterioration and duration management. The net realized gains or losses recognized by the Company related to such sales were not significant during the three- and six-month periods ended March 28, 2015 and March 29, 2014. The maturities of the Company s long-term marketable securities generally range from one to five years.

As of March 28, 2015 and September 27, 2014, gross unrealized losses related to individual securities that had been in a continuous loss position for 12 months or longer were not significant.

During the three- and six-month periods ended March 28, 2015 and March 29, 2014, the Company did not recognize any significant impairment charges. As of March 28, 2015, the Company considers the declines in market value of its marketable securities investment portfolio to be temporary in nature and does not consider any of its investments other-than-temporarily impaired. The Company typically invests in highly-rated securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy generally requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. When evaluating an investment for other-than-temporary impairment the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates and the Company s intent to sell, or whether it is more likely than not it will be required to sell the investment before recovery of the investment s cost basis.

Derivative Financial Instruments

The Company uses derivatives to partially offset its business exposure to foreign currency and interest rate risk on expected future cash flows, on net investments in certain foreign subsidiaries and on certain existing assets and liabilities. However, the Company may choose not to hedge certain exposures for a variety of reasons including, but not limited to, accounting considerations and the prohibitive economic cost of hedging particular exposures. There can be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in foreign currency exchange or interest rates.

To help protect gross margins from fluctuations in foreign currency exchange rates, certain of the Company s subsidiaries whose functional currency is the U.S. dollar may hedge a portion of forecasted foreign currency revenue, and subsidiaries whose functional currency is not the U.S. dollar and who sell in local currencies may hedge a portion of forecasted inventory purchases not denominated in the subsidiaries functional currencies. The Company may enter into forward contracts, option contracts or other instruments to manage this risk and may designate these instruments as cash flow hedges. The Company typically hedges portions of its forecasted foreign currency exposure associated with revenue and inventory purchases, typically for up to 12 months.

To help protect the net investment in a foreign operation from adverse changes in foreign currency exchange rates, the Company may enter into foreign currency forward and option contracts to offset the changes in the carrying amounts of these investments due to fluctuations in foreign currency exchange rates. The Company designates these instruments as net investment hedges.

The Company may also enter into non-designated foreign currency contracts to partially offset the foreign currency exchange gains and losses generated by the re-measurement of certain assets and liabilities denominated in non-functional currencies.

The Company may enter into interest rate swaps, options, or other instruments to manage interest rate risk. These instruments may offset a portion of changes in income or expense, or changes in fair value of the Company s long-term debt or investments. The Company designates these instruments as either cash flow or fair value hedges. The Company s hedged interest rate transactions as of March 28, 2015 are expected to be recognized within 12 years.

Cash Flow Hedges

The effective portions of cash flow hedges are recorded in accumulated other comprehensive income (AOCI) until the hedged item is recognized in earnings. Deferred gains and losses associated with cash flow hedges of foreign currency revenue are recognized as a component of net sales in the same period as the related revenue is recognized, and deferred gains and losses related to cash flow hedges of inventory purchases are recognized as a component of cost of sales in the same period as the related costs are recognized. Deferred gains and losses associated with cash flow hedges of interest income or expense are recognized in other income/(expense), net in the same period as the related income or expense is recognized.

The ineffective portions and amounts excluded from the effectiveness testing of cash flow hedges are recognized in other income/(expense), net. These amounts were not significant during the three- and six-month periods ended March 28, 2015 and March 29, 2014.

Table of Contents

Derivative instruments designated as cash flow hedges must be de-designated as hedges when it is probable the forecasted hedged transaction will not occur in the initially identified time period or within a subsequent two-month time period. Deferred gains and losses in AOCI associated with such derivative instruments are reclassified immediately into other income/(expense), net. Any subsequent changes in fair value of such derivative instruments are reflected in other income/(expense), net unless they are re-designated as hedges of other transactions. The Company did not recognize any significant net gains or losses related to the loss of hedge designation on discontinued cash flow hedges during the three- and six-month periods ended March 28, 2015 and March 29, 2014.

Net Investment Hedges

The effective portions of net investment hedges are recorded in other comprehensive income (OCI) as a part of the cumulative translation adjustment. The ineffective portions and amounts excluded from the effectiveness testing of net investment hedges are recognized in other income/(expense), net. These amounts were not significant during the three- and six-month periods ended March 28, 2015 and March 29, 2014.

Fair Value Hedges

Gains and losses related to changes in fair value hedges are recognized in earnings along with a corresponding loss or gain related to the change in value of the underlying hedged item. The ineffective portions and amounts excluded from the effectiveness testing of fair value hedges recognized were not significant during the three- and six-month periods ended March 28, 2015 and March 29, 2014.

Non-Designated Derivatives

Derivatives that are not designated as hedging instruments are adjusted to fair value through earnings in the financial statement line item to which the derivative relates. The net gains and losses recognized for foreign currency forward and option contracts not designated as hedging instruments were not significant during the three- and six-month periods ended March 28, 2015 and March 29, 2014.

The Company records all derivatives in the Condensed Consolidated Balance Sheets at fair value. The Company s accounting treatment for these derivative instruments is based on its hedge designation. The following tables show the Company s derivative instruments at gross fair value as of March 28, 2015 and September 27, 2014 (in millions):

		March 28, 2015	
	Fair Value of Derivatives Designated as Hedge Instruments	**Fair Value of Derivatives Not Designated as Hedge Instruments**	**Total Fair Value**
Derivative assets [1]:			
Foreign exchange contracts	$ 3,045	$ 86	$ 3,131
Interest rate contracts	$ 329	$ 0	$ 329
Derivative liabilities [2]:			
Foreign exchange contracts	$ 27	$ 91	$ 118
Interest rate contracts	$ 458	$ 0	$ 458

	September 27, 2014		
	Fair Value of Derivatives Designated as Hedge Instruments	Fair Value of Derivatives Not Designated as Hedge Instruments	Total Fair Value
Derivative assets [1]:			
Foreign exchange contracts	$ 1,332	$ 222	$ 1,554
Interest rate contracts	$ 81	$ 0	$ 81
Derivative liabilities [2]:			
Foreign exchange contracts	$ 41	$ 40	$ 81

(1) The fair value of derivative assets is measured using Level 2 fair value inputs and is recorded as other current assets in the Condensed Consolidated Balance Sheets.

(2) The fair value of derivative liabilities is measured using Level 2 fair value inputs and is recorded as accrued expenses in the Condensed Consolidated Balance Sheets.

Table of Contents

The following tables show the pre-tax gains and losses of the Company s derivative instruments designated as cash flow, net investment and fair value hedges on OCI and the Condensed Consolidated Statements of Operations for the three- and six-month periods ended March 28, 2015 and March 29, 2014 (in millions):

	Three Months Ended		Six Months Ended	
	March 28, 2015	March 29, 2014	March 28, 2015	March 29, 2014
Gains/(Losses) recognized in OCI effective portion:				
Cash flow hedges:				
Foreign exchange contracts	$ 1,591	$ (121)	$ 4,176	$ 143
Interest rate contracts	(429)	(27)	(517)	(6)
Total	$ 1,162	$ (148)	$ 3,659	$ 137
Net investment hedges:				
Foreign exchange contracts	$ (6)	$ (19)	$ 112	$ 5
Gains/(Losses) reclassified from AOCI into net income effective portion:				
Cash flow hedges:				
Foreign exchange contracts	$ 1,166	$ 22	$ 1,928	$ (52)
Interest rate contracts	(353)	(4)	(452)	(8)
Total	$ 813	$ 18	$ 1,476	$ (60)
Gains/(Losses) on derivative instruments:				
Fair value hedges:				
Interest rate contracts	$ 122	$ 0	$ 239	$ 0
Gains/(Losses) related to hedged items:				
Fair value hedges:				
Interest rate contracts	$ (122)	$ 0	$ (239)	$ 0

The following table shows the notional amounts of the Company s outstanding derivative instruments and credit risk amounts associated with outstanding or unsettled derivative instruments as of March 28, 2015 and September 27, 2014 (in millions):

	March 28, 2015		September 27, 2014	
	Notional Amount	**Credit Risk Amounts**	**Notional Amount**	**Credit Risk Amounts**
Instruments designated as accounting hedges:				
Foreign exchange contracts	$ 37,855	$ 3,045	$ 42,945	$ 1,333
Interest rate contracts	$ 18,013	$ 329	$ 12,000	$ 89
Instruments not designated as accounting hedges:				
Foreign exchange contracts	$ 27,486	$ 86	$ 38,510	$ 222

The notional amounts for outstanding derivative instruments provide one measure of the transaction volume outstanding and do not represent the amount of the Company s exposure to credit or market loss. The credit risk amounts represent the Company s gross exposure to potential accounting loss on derivative instruments that are outstanding or unsettled if all counterparties failed to perform according to the terms of the contract, based on then-current currency or interest rates at each respective date. The Company s exposure to credit loss and market risk will vary over time as currency and interest rates change. Although the table above reflects the notional and credit risk amounts of the Company s derivative instruments, it does not reflect the gains or losses associated with the exposures and transactions that the instruments are intended to hedge. The amounts ultimately realized upon settlement of these financial instruments, together with the gains and losses on the underlying exposures, will depend on actual market conditions during the remaining life of the instruments.

Table of Contents

The Company generally enters into master netting arrangements, which are designed to reduce credit risk by permitting net settlement of transactions with the same counterparty. To further limit credit risk, the Company generally enters into collateral security arrangements that provide for collateral to be received or posted when the net fair value of certain financial instruments fluctuates from contractually established thresholds. The Company presents its derivative assets and derivative liabilities at their gross fair values in its Condensed Consolidated Balance Sheets. As of March 28, 2015 and September 27, 2014, the Company received $3.7 billion and $2.1 billion, respectively, of cash collateral related to the derivative instruments under its collateral security arrangements, which were recorded as other current liabilities within accrued expenses in the Condensed Consolidated Balance Sheets. The Company did not have any derivative instruments with credit-risk related contingent features that would require it to post additional collateral as of March 28, 2015 and September 27, 2014.

Under master netting arrangements with the respective counterparties to the Company s derivative contracts, the Company is allowed to net settle transactions with a single net amount payable by one party to the other. As of March 28, 2015 and September 27, 2014, the potential effects of these rights of set-off associated with the Company s derivative contracts, including the effects of collateral, would be a reduction to both derivative assets and derivative liabilities of $3.6 billion and $1.6 billion, respectively, resulting in net derivative liabilities of $859 million and $549 million, respectively.

Accounts Receivable

Trade Receivables

The Company has considerable trade receivables outstanding with its third-party cellular network carriers, wholesalers, retailers, value-added resellers, small and mid-sized businesses and education, enterprise and government customers that are not covered by collateral, third-party financing arrangements or credit insurance. As of March 28, 2015, the Company had one customer that represented 10% or more of total trade receivables, which accounted for 11%. As of September 27, 2014, the Company had two customers that represented 10% or more of total trade receivables, one of which accounted for 16% and the other 13%. The Company s cellular network carriers accounted for 63% and 72% of trade receivables as of March 28, 2015 and September 27, 2014, respectively.

Vendor Non-Trade Receivables

Additionally, the Company has non-trade receivables from certain of its manufacturing vendors resulting from the sale of components to these vendors who manufacture sub-assemblies or assemble final products for the Company. Vendor non-trade receivables from three of the Company s vendors accounted for 48%, 18% and 16% of total vendor non-trade receivables as of March 28, 2015 and three of the Company s vendors accounted for 51%, 16% and 14% of total vendor non-trade receivables as of September 27, 2014.

Note 3 Condensed Consolidated Financial Statement Details

The following tables show the Company s condensed consolidated financial statement details as of March 28, 2015 and September 27, 2014 (in millions):

Inventories

	March 28, 2015	September 27, 2014
Components	$ 537	$ 471
Finished goods	1,859	1,640
Total inventories	$ 2,396	$ 2,111

Property, Plant and Equipment, Net

	March 28, 2015	September 27, 2014
Land and buildings	$ 5,627	$ 4,863
Machinery, equipment and internal-use software	32,107	29,639
Leasehold improvements	4,726	4,513
Gross property, plant and equipment	42,460	39,015
Accumulated depreciation and amortization	(22,309)	(18,391)
Total property, plant and equipment, net	$ 20,151	$ 20,624

Table of Contents

Accrued Expenses

	March 28, 2015	September 27, 2014
Accrued warranty and related costs	$ 5,143	$ 4,159
Accrued taxes	2,017	1,209
Accrued marketing and selling expenses	1,384	2,321
Accrued compensation and employee benefits	1,254	1,209
Deferred margin on component sales	1,130	1,057
Other current liabilities	11,899	8,498
Total accrued expenses	$ 22,827	$ 18,453

Other Non-Current Liabilities

	March 28, 2015	September 27, 2014
Deferred tax liabilities	$ 23,825	$ 20,259
Other non-current liabilities	5,991	4,567
Total other non-current liabilities	$ 29,816	$ 24,826

Other Income/(Expense), Net

The following table shows the detail of other income/(expense), net for the three- and six-month periods ended March 28, 2015 and March 29, 2014 (in millions):

	Three Months Ended		Six Months Ended	
	March 28, 2015	March 29, 2014	March 28, 2015	March 29, 2014
Interest and dividend income	$ 675	$ 410	$ 1,329	$ 837
Interest expense	(163)	(85)	(294)	(169)
Other expense, net	(226)	(100)	(579)	(197)
Total other income/(expense), net	$ 286	$ 225	$ 456	$ 471

Note 4 Goodwill and Other Intangible Assets

The Company s acquired intangible assets with definite useful lives primarily consist of patents and licenses and are amortized over periods typically from three to seven years. The following table summarizes the components of gross and net intangible asset balances as of March 28, 2015 and September 27, 2014 (in millions):

	March 28, 2015			September 27, 2014		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Definite-lived and amortizable acquired intangible assets	$ 7,672	$ (3,711)	$ 3,961	$ 7,127	$ (3,085)	$ 4,042
Indefinite-lived and non-amortizable acquired intangible assets	100	0	100	100	0	100
Total acquired intangible assets	$ 7,772	$ (3,711)	$ 4,061	$ 7,227	$ (3,085)	$ 4,142

Note 5 Income Taxes

As of March 28, 2015, the Company recorded gross unrecognized tax benefits of $4.6 billion, of which $1.6 billion, if recognized, would affect the Company s effective tax rate. As of September 27, 2014, the total amount of gross unrecognized tax benefits was $4.0 billion, of which $1.4 billion, if recognized, would have affected the Company s effective tax rate. The Company s total gross unrecognized tax benefits are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets. The Company had $844 million and $630 million of gross interest and penalties accrued as of March 28, 2015 and September 27, 2014, respectively, which are classified as other non-current liabilities in the Condensed Consolidated Balance Sheets.

Management believes that an adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in the Company s tax audits are resolved in a manner not consistent with management s expectations, the Company could be required to adjust its provision for income taxes in the period such resolution occurs. Although timing of the resolution and/or closure of audits is not certain, the Company does not believe it is reasonably possible that its unrecognized tax benefits would materially change in the next 12 months.

On June 11, 2014, the European Commission issued an opening decision initiating a formal investigation against Ireland for alleged state aid to the Company. The opening decision concerns the allocation of profits for taxation purposes of the Irish branches of two subsidiaries of the Company. The Company believes the European Commission s assertions are without merit. If the European Commission were to conclude against Ireland, the European Commission could require Ireland to recover from the Company past taxes covering a period of up to 10 years reflective of the disallowed state aid. While such amount could be material, as of March 28, 2015 the Company is unable to estimate the impact.

Note 6 Debt

Commercial Paper

In 2014, the Board of Directors authorized the Company to issue unsecured short-term promissory notes (Commercial Paper) pursuant to a commercial paper program. The Company intends to use net proceeds from the commercial paper program for general corporate purposes, including dividends and share repurchases. As of March 28, 2015 and September 27, 2014, the Company had $3.8 billion and $6.3 billion of Commercial Paper outstanding, respectively, with a weighted-average interest rate of 0.10% and 0.12%, respectively, and maturities generally less than nine months.

The following table provides a summary of cash flows associated with the issuance and maturities of Commercial Paper for the six months ended March 28, 2015 (in millions):

Maturities less than 90 days:		
Proceeds from (repayments of) commercial paper, net	$	985
Maturities greater than 90 days:		
Proceeds from commercial paper		547
Repayments of commercial paper		(4,040)

Maturities greater than 90 days, net		(3,493)
Total repayments of commercial paper, net	$	(2,508)

14

Table of Contents

Long-Term Debt

As of March 28, 2015, the Company has outstanding floating- and fixed-rate notes with varying maturities for an aggregate principal amount of $39.9 billion (collectively the Notes). The Notes are senior unsecured obligations, and interest is payable in arrears, quarterly for the domestic floating-rate notes, semi-annually for the domestic fixed-rate notes and annually for the foreign fixed-rate notes. The following table provides a summary of the Company s long-term debt as of March 28, 2015 and September 27, 2014:

	March 28, 2015		September 27, 2014	
	Amount (in millions)	Effective Interest Rate	Amount (in millions)	Effective Interest Rat
ting-rate notes due 2016 [1]	$ 1,000	0.51%	$ 1,000	0.5
ting-rate notes due 2017 [2]	1,000	0.33%	1,000	0.3
ting-rate notes due 2018 [1]	2,000	1.10%	2,000	1.1
ting-rate notes due 2019 [2]	1,000	0.56%	1,000	0.5
ting-rate notes due 2020 [3]	500	0.51%	0	
d-rate 0.45% notes due 2016 [1]	1,500	0.51%	1,500	0.5
d-rate 1.05% notes due 2017 [2]	1,500	0.32%	1,500	0.3
d-rate 1.00% notes due 2018 [1]	4,000	1.08%	4,000	1.0
d-rate 2.10% notes due 2019 [2]	2,000	0.55%	2,000	0.5
d-rate 1.55% notes due 2020 [3]	1,250	0.50%	0	
d-rate 2.85% notes due 2021 [2]	3,000	0.81%	3,000	0.7
d-rate 2.15% notes due 2022 [3]	1,250	0.82%	0	
d-rate 1.00% Euro-denominated notes due 2022 [4]	1,534	2.94%	0	
d-rate 2.40% notes due 2023 [1]	5,500	2.44%	5,500	2.4
d-rate 3.45% notes due 2024 [2]	2,500	0.92%	2,500	0.9
d-rate 0.38% Swiss Franc-denominated notes due 2024 [5]	915	0.28%	0	
d-rate 2.50% notes due 2025 [3]	1,500	2.60%	0	
d-rate 1.63% Euro-denominated notes due 2026 [4]	1,534	3.45%	0	
d-rate 0.75% Swiss Franc-denominated notes due 2030 [5]	392	0.74%	0	
d-rate 3.85% notes due 2043 [1]	3,000	3.91%	3,000	3.9
d-rate 4.45% notes due 2044 [2]	1,000	4.48%	1,000	4.4
d-rate 3.45% notes due 2045 [3]	2,000	3.58%	0	
l borrowings	39,875		29,000	
mortized discount	(80)		(52)	
ge accounting fair value adjustments	277		39	
l long-term debt	$ 40,072		$ 28,987	

(1) Tranche relates to the $17.0 billion debt issuance in the third quarter of 2013.

(2) Tranche relates to the $12.0 billion debt issuance in the third quarter of 2014.

(3) Tranche relates to the $6.5 billion debt issuance in the second quarter of 2015.

(4) Tranche relates to Euro-denominated debt issuance of 2.8 billion in the first quarter of 2015.

(5) Tranche relates to Swiss Franc-denominated debt issuance of SFr1.3 billion in the second quarter of 2015.

During the first six months of 2015, the Company issued 2.8 billion of Euro-denominated notes, $6.5 billion of U.S. dollar-denominated notes and SFr1.3 billion of Swiss Franc-denominated notes. To manage foreign currency risk associated with the Euro-denominated notes, the Company entered into currency swaps with an aggregate notional amount of $3.5 billion, which effectively converted the Euro-denominated notes to U.S. dollar-denominated notes. To manage interest rate risk on the U.S. dollar-denominated fixed-rate notes maturing in 2020 and 2022, the Company entered into interest rate swaps with an aggregate notional amount of $2.5 billion, which effectively converted the fixed interest rates on these notes to a floating interest rate. For further discussion regarding the Company s use of derivative instruments to manage interest rate and foreign currency risk, see the Derivative Financial Instruments section of Note 2, Financial Instruments.

Table of Contents

The effective interest rates for the Notes include the interest on the Notes, amortization of the discount and, if applicable, adjustments related to hedging. The Company recognized $161 million and $289 million of interest expense on its long-term debt for the three- and six-month periods ended March 28, 2015, respectively. The Company recognized $84 million and $168 million of interest expense on its long-term debt for the three- and six-month periods ended March 29, 2014, respectively.

Future principal payments for the Company s Notes as of March 28, 2015 are as follows (in millions):

2015	$	0
2016		2,500
2017		2,500
2018		6,000
2019		3,000
Thereafter		25,875
Total future principal payments	$	39,875

As of March 28, 2015 and September 27, 2014, the fair value of the Company s Notes, based on Level 2 inputs, was $40.2 billion and $28.5 billion, respectively.

Note 7 Shareholders Equity

Dividends

The Company declared and paid cash dividends per share during the periods presented as follows:

		Dividends Per Share		**Amount** (in millions)
2015:				
Second quarter	$	0.47	$	2,734
First quarter		0.47		2,750
Total cash dividends declared and paid	$	0.94	$	5,484
2014:				
Fourth quarter	$	0.47	$	2,807
Third quarter		0.47		2,830
Second quarter		0.44		2,655
First quarter		0.44		2,739
Total cash dividends declared and paid	$	1.82	$	11,031

Future dividends are subject to declaration by the Board of Directors.

Share Repurchase Program

In 2014, the Company s Board of Directors increased the share repurchase authorization to $90 billion of the Company s common stock, of which $80.0 billion had been utilized as of March 28, 2015. The Company s share repurchase program does not obligate it to acquire any specific number of shares. Under the program, shares may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended (the Exchange Act).

The Company has entered, and in the future may enter, into accelerated share repurchase arrangements (ASRs) with financial institutions. In exchange for up-front payments, the financial institutions deliver shares of the Company s common stock during the purchase periods of each ASR. The total number of shares ultimately delivered, and therefore the average repurchase price paid per share, is determined at the end of the applicable purchase period of each ASR based on the volume weighted-average price of the Company s common stock during that period. The shares received are retired in the periods they are delivered, and the up-front payments are accounted for as a reduction to shareholders equity in the Company s Condensed Consolidated Balance Sheet in the periods the payments are made. The Company reflects the ASRs as a repurchase of common stock in the period delivered for purposes of calculating earnings per share and as forward contracts indexed to its own common stock. The ASRs met all of the applicable criteria for equity classification, and therefore, were not accounted for as derivative instruments.

The following table shows the Company s ASR activity and related information during the six months ended March 28, 2015 and the year ended September 27, 2014:

	Purchase Period End Date	Number of Shares (in thousands)	Average Repurchase Price Per Share	ASR Amount (in millions)
August 2014 ASR	February 2015	81,525 [(1)]	$ 110.40	$ 9,000
January 2014 ASR	December 2014	134,247	$ 89.39	$ 12,000
April 2013 ASR	March 2014	172,548	$ 69.55	$ 12,000

(1) Includes 59.9 million shares delivered and retired at the beginning of the purchase period, which began in the fourth quarter of 2014, 8.3 million net shares delivered and retired in the first quarter of 2015 and 13.3 million shares delivered and retired at the end of the purchase period, which concluded in the second quarter of 2015.

Additionally, the Company repurchased shares of its common stock in the open market, which were retired upon repurchase, during the periods presented as follows:

	Number of Shares (in thousands)	Average Repurchase Price Per Share	Amount (in millions)
2015:			
Second quarter	56,400	$ 124.11	$ 7,000
First quarter	45,704	$ 109.40	5,000
Total open market common stock repurchases	102,104		$ 12,000
2014:			
Fourth quarter	81,255	$ 98.46	$ 8,000
Third quarter	58,661	$ 85.23	5,000
Second quarter	79,749	$ 75.24	6,000
First quarter	66,847	$ 74.79	5,000
Total open market common stock repurchases	286,512		$ 24,000

Note 8 Comprehensive Income

Comprehensive income consists of two components, net income and OCI. OCI refers to revenue, expenses, and gains and losses that under GAAP are recorded as an element of shareholders equity but are excluded from net income. The Company s OCI consists of foreign currency translation adjustments from those subsidiaries not using the U.S. dollar as their functional currency, net deferred gains and losses on certain derivative instruments accounted for as cash flow hedges and unrealized gains and losses on marketable securities classified as available-for-sale.

The following table shows the pre-tax amounts reclassified from AOCI into the Condensed Consolidated Statements of Operations, and the associated financial statement line item, for the three- and six-month periods ended March 28, 2015 and March 29, 2014 (in millions):

		Three Months Ended		Six Months Ended	
Comprehensive Income Components	**Financial Statement Line Item**	**March 28, 2015**	**March 29, 2014**	**March 28, 2015**	**March 29, 2014**
Unrealized (gains)/losses on derivative instruments:					
Foreign exchange contracts	Revenue	$ (558)	$ 119	$ (1,007)	$ 303
	Cost of sales	(608)	(141)	(921)	(251)
	Other income/(expense), net	(1)	4	(1)	14
Interest rate contracts	Other income/(expense), net	353	4	452	8
		(814)	(14)	(1,477)	74
Unrealized (gains)/losses on marketable securities	Other income/(expense), net	56	(60)	34	(77)
Total amounts reclassified from AOCI		$ (758)	$ (74)	$ (1,443)	$ (3)

Table of Contents

The following table shows the changes in AOCI by component for the six months ended March 28, 2015 (in millions):